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KEYNES' ECONOMIC CONSEQUENCES OF THE PEACE¹

John Maynard Keynes is a son of John Neville Keynes, the author of a standard treatise on *The Scope and Method of Political Economy*; he has followed his father's career at Cambridge, is a fellow of King's College, and is one of the editors of the *Economic Journal*. He was in charge of British financial relations with the Allied Powers during the war, and in 1917 accompanied Lord Reading to Washington as financial adviser. At the Peace Conference he was the chief representative of the British Treasury, having been prepared for this responsible position not only by his previous war activities, but by his earlier service of ten years in the British Civil Service, in the India Office and Treasury. As alternate for Mr. Austen Chamberlain, who was rarely in Paris, he had a seat on the Supreme Economic Council, and was further a member of the Commission on Financial Questions, sitting on the sub-commission charged with the consideration of urgent problems relating to the preliminaries of peace. He resigned from his official positions when he lost hope of an amendment of the terms of peace; and he sets forth in this book the grounds of his objections to the policy of the conference and to the treaty which it framed.

The book has had a large sale both in England and in the United States. It was published in this country in the last week of January and a publisher's circular of March 8 asserts that the first printing of 20,000 copies had been sold, and that another large edition (apparently of 30,000) was being distributed. Nine translations of the book are said to be in process of preparation. It has been the text of discussion in the House of Commons and in the Senate, has been the subject of unofficial protests by French officials, has been debated on the platform, reviewed widely, and discussed everywhere.

The reasons for the unusual attention which the book has enjoyed are not far to seek. It treats a question which is constantly alive in the minds of thoughtful men: what is to become of Europe in the issue from the great war? It challenges the official solution proposed by the Peace Conference in the German treaty, and, under threats of the gravest consequences, demands a revision of

¹ JOHN MAYNARD KEYNES: *The Economic Consequences of the Peace*. (New York: Harcourt, Brace and Howe. 1920. Pp. 298.)

the terms. The author seeks by an appeal to public opinion to accomplish what he and others of like views were unable to effect at the conference itself. He states the facts with the authority of one whose official responsibility it was to know the facts and to understand their bearing. He exposes the situation with the skill of the trained economist. Finally, he presents his case with an art which keeps the official and the academic theorist in the background. The terms of the treaty, the intricate features of the reparation arrangements, and their probable consequences are not presented until the attention of the reader has been won by other aspects of the conference, less abstract, and strongly personal.

The first three chapters are altogether theatrical. Even a description of the economic organization of Europe before the war takes on this cast. The workaday world appears, as it has appeared before to gloomy observers in many earlier periods, "intensely unusual, unstable, complicated, unreliable, temporary." Familiar figures appear in strained positions. It is like a drawing by Gustave Doré, with its exaggerations, its heavy shadows, its implication of something horrible in the background. The Paris of the Conference is shown in all the trappings of the theatre. "Paris was a nightmare, and everyone there was morbid. A sense of impending catastrophe overhung the frivolous scene; the futility and smallness of man before the great events confronting him; the mingled significance and unreality of the decisions; levity, blindness, insolence, confused cries from without,—all the elements of ancient tragedy were there." The conference resolves itself into the conflict for mastery of three great personalities, Clemenceau, Lloyd George, and Wilson. We see Clemenceau, "throned, in his gray gloves, on the brocade chair, dry in soul and empty of hope, very old and tired, but surveying the scene with a cynical and almost impish air," resolute to secure for France the Carthaginian Peace which would remove to an indefinite future the danger of a strong Germany on her eastern frontier. We see "the British Prime Minister watching the company with six or seven senses not available to ordinary men, judging character, motive, and subconscious impulse, perceiving what each was thinking and even what each was going to say next, and compounding with telepathic instinct the argument or appeal best suited to the vanity, weakness, or self-interest of his immediate auditor." Pitted against these two men we see the President, "the

man of destiny who, coming from the west, was to bring healing to the wounds of the ancient parent of his civilization and lay for us the foundations of the future," "the philosopher-king," who, as the event proved, alas, "was not a hero or a prophet; he was not even a philosopher; but a generously intentioned man, with many of the weaknesses of other human beings, and lacking that dominating intellectual equipment which would have been necessary to cope with the subtle and dangerous spell-binders whom a tremendous clash of forces and personalities had brought to the top as triumphant masters in the swift game of give and take, face to face in Council,—a game of which he had no experience at all."

When one has begun to quote from this part of the book, one finds it hard to stop. Those who have read the book will forgive me, I am sure, for recalling to their minds some of its extraordinary bits of personal portraiture; those who have not read it can be assured that they will not find in novel or play a more absorbing study of character or more sustained interest than it presents throughout, to that closing passage in which the author shows why "it was harder to de-bamboozle this old Presbyterian than it had been to bamboozle him."

I have another object, however, than the mere relish for effective writing, in quoting these passages. They characterize the book. It is written by an economist on an economic subject, but it is not, and cannot have been designed to be, a contribution to economic literature. It is a political tract. Like the writings of Daniel Defoe and the *British Merchant* on the Peace of Utrecht, two hundred years ago, it is meant to rouse public interest and to force political action, and to reach that end it follows methods which are far removed from those of the strict scientist.

It is the more remarkable, and much to the author's credit, that the body of the book, discussing the terms of the treaty and of the reparation payment, is sober and trustworthy. Every little while the author gives evidence of strong feeling, and occasionally he lets his feeling color his judgment. I shall refer later to instances. In general he is perfectly fair in distinguishing statements of opinion from statements of fact, and in stating facts for and against his case. And on the basis of fact he establishes beyond reasonable doubt, it seems to me, the two main points in his case; first, that the terms of the treaty *may* involve a serious breach of faith on the part of the allies; second, that the reparations to be exacted *may* be far beyond the capacity of the Germans to pay.

The first of these points involves a consideration of the principles of settlement embodied in the public addresses of the President before the Armistice. There is here, as always, an opening for a difference of opinion between the strict constructionist and the loose constructionist, but I agree with Keynes in thinking that the intent of certain passages is unmistakable: "No annexations, no contributions, no punitive damages," but payment for "all damage done to the civil population of the Allies and to their property by the aggression of Germany by land, by sea, and from the air." With the spirit of such passages the terms imposed on Germany must be made to square.

With those provisions the terms of the treaty, in the form they *may* take, cannot be made to square. I state my opinion in bald form and without attempt at argument. Furthermore the terms of reparation *may* be construed so far as to lay on Germany an impossible burden. It is impracticable here to discuss the matter in full detail, but Keynes' treatment of it is by far the most important contribution of his book, and deserves at least some illustration and comment.

The treaty, it will be remembered, did not specify a definite sum due from Germany for reparation. Germany accepted full responsibility for all the loss and damage resulting from the war, and was made to sign, as has been said, a blank check covering not merely damage to civilian population defined in the quotation from the pre-Armistice conditions just above, but further "in general all damage as defined in Annex I" of the treaty. In this Annex is inserted the claim for the amount of separation allowances and pensions paid by the allied and associated governments. The amount which would be due under this head is so enormous that the issue of justice and expediency practically depends on the issue of this claim.

The author estimates the amount due under a strict construction of the pre-Armistice conditions, as follows:

Belgium	\$2,500,000,000
France	4,000,000,000
Great Britain	2,850,000,000
Other Allies	1,250,000,000
Total	<hr/> \$10,600,000,000

The author presents in considerable detail the material and the processes by which he reached his final estimate. I have not the means of checking the figures. Personally I find an entirely satis-

factory guarantee for the honesty of the author in this part of his work, and for the general acceptability of his conclusions, in the fact that two American economists, Taussig and Young, who are qualified not only by their general standing as scholars but in particular by their official experience in the economic work of the American Peace Commission, have passed upon the work, and express, for this part of it, nothing but respect. There is, it is true, an almost indefinite allowance for possible error to be made in work of this kind. Young, for example, would put the figure of losses under this head nearer twenty billion than ten. The spread between these two sums appears enormous, when they are taken as measures of what Germany must or can pay. The difference appears of little account when it is put alongside the additional sum for which Germany may be held responsible under Annex I of the reparation provisions.

The author's estimate ("guess," he calls it) of amount due under this head, is as follows:

British Empire	\$7,000,000,000
France	12,000,000,000
Italy	2,500,000,000
Others (including United States).....	3,500,000,000
Total	<u>\$25,000,000,000</u>

The gross sum due from Germany would therefore be about \$40,000,000,000. "As a matter of subjective judgment," the author says, "I estimate for this figure an accuracy of 10 per cent in deficiency and 20 per cent in excess, *i.e.*, that the result will lie between \$32,000,000,000 and \$44,000,000,000."

The treaty leaves indefinite not only the total sum due from Germany, but also the periods of payments of some parts of it and other data which are of the first importance if one seeks to arrive at a figure which will summarize the extent of the financial burden which may be imposed. It is unprofitable to examine all the various possibilities, but it is interesting to view the outcome conceivable as resulting from a rigorous exaction of the obligation which Germany has assumed.

On the assumption that Germany cannot pay more than \$750,000,000 annually until 1936 (*i.e.*, 5 per cent interest on \$15,000,000,000) the \$25,000,000,000 on which interest is deferred will have risen to \$50,000,000,000, carrying an annual interest charge of \$2,500,000,000. That is to say, even if Germany pays \$750,000,000 annually up to 1936, she will nevertheless owe us at that date more than half as much again as she does now (\$65,000,000,000 as compared with \$40,-

000,000,000). From 1936 onwards she will have to pay to us \$3,250,000,000 annually in order to keep pace with the interest alone. At the end of any year in which she pays less than this sum, she will owe more than she did at the beginning of it. And if she is to discharge this capital sum in thirty years from 1936, *i.e.*, in forty-eight years from the Armistice, she must pay an additional \$650,000,000 annually, making \$3,900,000,000 in all.

Clearly we are here in a world of unrealities and must abandon it, as of course the Conference should have abandoned it, to consider the practical question: What *can* Germany pay? The author concludes, after an examination of German assets, and of the possible surplus of productive power available for credit abroad, that the country can pay at most \$500,000,000 a year. Annual payments of this amount, allowing 5 per cent for interest, and 1 per cent for repayment of capital, continued for thirty years, represent a present value of about \$8,500,000,000.

The process by which the author reaches this conclusion appears to me open to criticism in detail. He assumes, for example, that Upper Silesia is irrevocably lost to Germany, a fact which remains to be determined; he appears to charge off all earning power based on the use of Silesian coal, again an unwarranted hypothesis; and I have failed to find any corresponding credit allowed for a reduction in the demand for imported goods which would follow a territorial cession. His view, throughout, is that of a pessimist; he finds it hard to see how production in this, that, or the other line can be increased or even maintained; he finds it hard to see how consumption can be reduced without immediate reaction on productive capacity. Over against his estimate of \$500,000,000 may be set the estimates of impartial American economists like Taussig and Young, approaching one billion dollars as a maximum. This same figure (four billion gold marks) is the conclusion of another American economist, H. C. Emery, who studied the question from the standpoint of the professional banker. Yet differences even of this magnitude may be reconciled, for they often result from a difference in premises. The American estimate of one billion dollars is avowedly a maximum, to be conceived as possible only under favoring conditions, and the developments of the last months have not promised well. All these estimates are of necessity based on statistics of German production dating from before the war, and it becomes more and more apparent with the passage of time that these statistics must be used with extreme caution in seeking an index of the productive

capacity of the immediate future. While the author has, I think, shown some bias in the use of the economic statistics, he has not demanded an allowance nearly as great as should be accorded him for the general demoralization which has become apparent. The question of what the Germans "can" pay involves social and political factors which are going to have immensely more influence on the sum that Germany actually does pay than are economic theories or antiquated economic facts.

What, then, is to be done? In the forefront of Keynes' program stands a revision of the treaty which will fix a definite sum due from Germany for reparation, within the limit of what Germany can reasonably be expected to pay. American representatives at the conference advocated this plan from the beginning, fought for it as long as there appeared any hope of its adoption, yielded to the insistence of the French and British only to get some agreement, and one which was not irrevocably bad, and refused to follow the British when they changed face at the last moment because to do so would have imperilled all the constructive work that had been done by the conference in other fields and gave no assurance of a satisfactory economic settlement in the face of French opposition.

"The representatives of the United States were greatly at fault, in my judgment," writes Keynes, "for having no constructive proposals whatever to offer to a suffering and distracted Europe." This should be compared with the sentences almost immediately preceding it. Keynes describes the personal and political factors which gave their final form to the terms of reparation in the treaty, and continues as follows: "The expectation which the exigencies of politics had made it necessary to raise were so very remote from the truth that a slight distortion of figures was no use, and it was necessary to ignore the facts entirely. The resulting unveracity was fundamental. On a basis of so much falsehood it became impossible to erect any constructive financial policy which was workable."

The terms of reparation fixed by the treaty were thoroughly bad, but they offered hope of amendment. The conviction that they must be amended, and must be radically amended, has grown steadily stronger since the signing of the peace, and there is no doubt that Keynes' book must be credited with a powerful contribution to this movement. Indications at the time of writing are that even the French will be brought in time to recognize the

necessity of fixing the reparation payment at a definite sum which Germany can be expected to pay within a reasonable time. What shall this sum be?

The author's estimate of \$8,500,000,000, present value, as the most that could be hoped for, has already been quoted. In the settlement that he suggests this figure does not appear, and the method that he follows in his proposal has subjected him to some criticism. He starts by allowing \$10,000,000,000 for reparation and for the costs of the army of occupation. These costs he has estimated, when discussing the treaty, at about \$1,000,000,000, and according to the treaty, of course, payments of these costs were not to be credited to reparation. Then he reckons various credits (ships, cables, war materials, claims, etc.) as worth the lump sum of \$2,500,000,000. "The balance of \$7,500,000,000 should not carry interest pending its repayment, and should be paid by Germany in thirty annual installments of \$250,000,000, beginning in 1923."

A "balance of \$7,500,000,000" paid under these conditions represents, of course, when discounted, a present value vastly less than the face of the figures. The amount of cash to be got from Germany under these terms appears pitifully small when compared with the just claims for reparation against that country, and it is a fair presumption that the author has stated his proposal in the form he chose because of that fact. Yet in discussing the counter-proposals of the Germans in an earlier chapter, he condemned them because "they exercised their ingenuity to produce a formula which might be represented to Allied opinion as yielding this [certain] amount, whilst really representing a much more modest sum"; he called their proposals "rather disingenuous," but "transparent," and thought "this subtlety did not benefit them and they would have done much better with a straightforward and candid estimate." The question of propriety and of policy involved gives the curious some stimulus to conjecture, but it is, of course, a matter of small moment. The vital question again is, how much can Germany pay and will Germany pay? My own guess is that the Allies, when they come (as they must) to fix a sum, will far exceed the figures that Keynes proposes, and that in the outcome they will get even less than he would give them. The reasons for this opinion are not, however, appropriate to the pages of an economic journal.

Second in importance among the author's remedies is the can-

cellation of the indebtedness between the governments of the allied and associated countries which was incurred for the purposes of the war. This proposal is one which he believes to be "absolutely essential to the future prosperity of the world." This proposal would, according to his figures, and leaving some doubtful items out of account, affect paper assets as follows, stating figures in round billions of dollars: the United States would lose 10 and the United Kingdom 4.5; France would gain 3.5 and Italy 4.

The author makes an eloquent plea for this settlement, and there is much in his argument which I believe to be entirely sound. He is surely justified in his confidence in the generosity of the American people, and may rightly assume that when the United States advanced the money "it was not in the nature of an investment." In one sense it was not. The American people paid out the money gladly during the war with little thought of the return to them of interest and principal. They expected a return, however, in the form of justice and decency and order. It seems to me highly improbable that they would, under present conditions, condone the act of their government, if, with a fine gesture, it renounced its claims, and gave up what hold it has on the governments of Europe. Most Americans would probably be willing to lose the money, but they would be quite unwilling to have it used to finance militarist and imperialist enterprises. "If I had interest at the United States Treasury," writes Keynes, "I would not lend a penny to a single one of the present governments of Europe." Most readers will agree with him; and most readers will want to wait awhile before they are ready to assent to the forgiving of debts already incurred.

Other remedies for the situation proposed by the author are not of serious importance. He would safeguard the provision of coal and iron to the Germans, and would amend the treaty to that end. He exaggerates, in my opinion, the effect which the new political frontiers of the treaty will have on the distribution of these important raw materials. Silesian coal, for example, was exported in large quantities to Austria before the war, in spite of a frontier to cross, and the Silesian coal interests were complaining (!) of the invasion of their market in northern Germany by British coal brought in from the sea. There are, of course, possible dangers in the situation resulting from the treaty, and I shall refer to one aspect of them immediately, but they do not appear so definite and so imminent as to justify specific measures for

averting them. A recent incident illustrates the difficulty of legislating on such matters. A provision of the treaty, which Keynes approves and would retain, requires Germany to furnish to France each year an amount of coal equal to the difference between the production of the mines in the northern departments before the war and in the current year. A news despatch announced not long ago that the miners of the Pas de Calais had gone on strike, and it is surely absurd that the French can now look to the German miners to make up for this deficiency in addition to the regular obligation which properly lies upon them.

One proposal of the author is extraordinary.

A Free Trade Union should be established under the auspices of the League of Nations of countries undertaking to impose no protectionist tariffs whatever against the produce of other members of the Union. Germany, Poland, the new states which formerly composed the Austro-Hungarian and Turkish Empires, and the Mandated states, should be compelled to adhere to this union for ten years, after which time adherence would be voluntary. The adherence of other states would be voluntary from the outset.

The objection which I should raise to this proposal is not that which I have seen made, that it is a realization of Naumann's "Central Europe." The scheme of Central Europe was a menace before the war, because of the military power behind it, but the old plan is as dead as Hamlet. I see no serious political danger in the new plan, and it offers economic benefit, almost unmixed, to the people who are included and to those who choose to share its advantages. One of the most serious dangers threatening the revival of central and eastern Europe is the splintering of the great empires, and the particularist tendencies in economic policy of the little states into which they have been shattered.

On the other hand one must be blind to political history not to realize that the little states wanted independence just so that each might pursue its own policy. It is instructive to note the restiveness inside the former empire of Austria-Hungary, and to realize that Hungary had advanced a long way toward a tariff against Austria before the dissolution of the monarchy was conceived as possible. To the economist, the thought of Europe being cut up into little units, each striving to be more or less self-sufficient, is abhorrent. Yet to that thought we must seek to reconcile ourselves. Politics and economics do not always march together. In the Austrian group of treaties the conference inserted

provisions designed to prevent the new states from abusing their independence in framing their commercial policy, but if it seeks to deny them a policy altogether it will certainly have to provide the League of Nations with an army to enforce its injunctions.

I cannot close this review without returning to the consideration of the first three chapters of the book, that part which I termed theatrical, and assumed to have been written to attract attention to the author's serious proposals. Some assumption of the kind must be made to excuse the introductory chapters, for if one disregards their art and attends to their substance one finds a description of the working of the conference and an explanation of its outcome which at best are superficial and which in many points are distorted and misleading. Yet this part of the book is that which has been most energetically advertised and most widely discussed, and this part is likely to make the deepest impression on the minds of readers. When I read in a sober journal like the *Contemporary Review* that Keynes' sketches "will be studied by historians for the next century," I am aghast at the mischief which may be done by a device which I believe to be legitimate in the work of the political pamphleteer, but which is poisonous when it is accepted as a contribution to history.

Keynes' analysis of the conference is superficial in two respects of importance. In the first place he neglects entirely the work of the conference outside that part of the field in which he is most interested, and in which its work was least satisfactory. Of the constructive work even in the economic field he sees only the flaws, and he assumes the League of Nations as a matter of course, without a recognition of the difficulty of establishing the covenant. Most noteworthy is his attitude to the territorial settlements which engaged so much of the time and energy of the conference. I do not recall a single passage in the book in which he shows an appreciation of the fact that these settlements were constructive work of the first magnitude, both in difficulty and in importance, and that these settlements were a prime condition of peace, of demobilization, of economic recovery.

In the second place, he gives the impression that the treaty was determined by the three heads of state, Clemenceau, Lloyd George, Wilson. It is certainly true that the power of final decision rested with the heads of state. It is true that some of the organs of the conference had only the appearance of power, and made relatively small contribution to the final issue. On the other

hand, work was constantly in progress in the background which in most matters of importance was of determining influence on the substance of the final outcome. The many commissions, of which some sat for months and in some periods held sessions on every working day and on some Sundays, sifted the facts, discussed the possibilities, and generally determined the limits within which a settlement would lie. It is true that the representatives of a certain country on a commission might be acting under instructions from their superiors, but these instructions were themselves moulded to suit the line that the commission as a whole was taking. The result, as it appears in the treaties, was not determined by a few outstanding persons, but was a composite to which many had contributed. An individual must, of course, be careful not to generalize from his own experience. My work lay almost entirely in the territorial field. In that I could trace the course of a question from its origin in the Council of Ten through a commission to its settlement in the Council of Four. On one occasion only, when the subjects for consideration overlapped, was I present at a session of the Four in the President's house when an economic question was under discussion. But on this occasion, at least, I had a demonstration that the technical advisers took an even more prominent and active part in the decision of economic issues than similar representatives took in the territorial field. And I am informed by active participants in the economic section that my general impression of the course of business in the conference is not mistaken.

Not only do I take exception to Keynes' theory of the working of the conference; if the book is to be regarded as a contribution to history, I must protest against the kind of history he chooses to write. "If an educated man were giving an account of the last change of administration," wrote Macaulay in 1828, "he would say—'Lord Goderich resigned; and the King, in consequence, sent for the Duke of Wellington.' A porter tells the story as if he had been hidden behind the curtains of the royal bed at Windsor: "So Lord Goderich says, 'I cannot manage this business, I must go out.' So the King says, says he,—'Well, then I must send for the Duke of Wellington, that's all.'"

Keynes does not, it is true, tell what his characters said, but he does more than that; he tells what they thought. Like Herodotus, of whom Macaulay was writing, he makes his appeal to "a nation susceptible, curious, lively, insatiably desirous of novelty and excite-

ment." The success of the appeal is undeniable. But I should as soon think of accepting Herodotus' account of the ants in India (larger than foxes but smaller than large dogs) as of accepting Keynes' account of the conference.

It is most unfortunate that it has suited the author's purpose, for reasons which I cannot understand but which I suppose to have to do with dramatic art, to distort as he has done the leading characters of the conference. I have no ground for refusing to accept the picture of Lloyd George. Clemenceau appears to me to be exalted above the position which he actually occupied. He did not know the facts. He was a picturesque figure, speaking with a decisive voice, but I suspect that other people told him what to say. Tardieu was a power on the French side who is not even mentioned in the book. But it is, of course, the President, who suffers most. He had enunciated the principles of a just peace; he is made responsible for any departure from them; the explanation is sought in weakness of intellect or character.

The author's philosophy of the conference is very simple. He distinguishes "the inevitable fruits of the war and the avoidable misfortunes of the peace." The flaws of the settlement would have been avoided, in his opinion, if the President had had the courage and ability to force his colleagues of the Four to carry out the pledges given before the Armistice. "The realities of power were in his hands." "But, if ever the action of a single individual matters, the collapse of the President has been one of the decisive moral events of history." He was a prey to the powerful resolution of Clemenceau and the wiles of Lloyd George, salved his conscience with the casuistry of a theologian, and capitulated.

I shall not follow the author's intricate analysis of the President's personality; much of it is beyond the threshold of the knowable. One or two positive mistakes can be corrected. The President, so far from "entering the cavern" a "deaf and blind Don Quixote," had a very definite appreciation of the difficulties and dangers confronting him, and took the pains to explain them to his subordinates before the conference opened. The President, so far from having a mind "slow and unadaptable," showed a quickness of perception, an ability to get a point and apply it, which was extraordinary; I believe that I am justified in asserting the author's contrary impression to be mistaken, since the American opinion on this point was shared by some of the British advisers, who compared the President and Lloyd George much to

the latter's disadvantage. It is unprofitable to continue a discussion along this line.

The fact of the matter is that no man on earth (not even, I venture to say, "the only man who emerged from the ordeal of Paris with an enhanced reputation," Mr. Hoover) could compose the conflicting interests and win a perfect peace. The President, in the opinion of the American advisers with whom I discussed the question, did more than any other man could have done; but he was not omnipotent. The forces against him were too powerful. The author himself recognizes this fact. He discusses possible courses open to the President when the French and British refused obstinately to be moved from their position. He finds none that promised a better issue.

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